Sunset Public Hearing Answers from
The Department of Financial Institutions
Created by Section 4-3-101, *Tennessee Code Annotated*
(Sunset termination June 2017)

Question 1: Provide a brief introduction to the Department of Financial Institutions, including information about its purpose, organization, statutory responsibilities and staff.

Answer: As of 9-30-16, the Department regulates 142 banks, 87 credit unions, 10 public trust companies, 1 business and industrial development corporation, 1,442 industrial loan and thrift companies, 50 insurance premium finance companies, 621 mortgage companies, 11,089 mortgage loan originators, 901 title pledge lenders, 568 check cashers, 1,044 deferred presentment services companies, 106 money transmitters and 564 flexible credit act lenders.

The Department plays a vital role in regulating and supporting the financial services industry and ensuring that Tennessee financial institutions remain fiscally strong and comply with governing authority.

The Department's mission is to ensure a safe and sound system of state-chartered institutions for Tennessee citizens, while giving institutions the opportunity to contribute to economic progress. In short, we seek to find balanced regulation. The condition of the Tennessee banking system continues to improve from the economic downturn. Tennessee state-chartered depository institutions remain well positioned to continue serving their communities.

Although continued consolidation within the banking industry is anticipated, total loans and assets continue to increase and the complexity and breadth of operations continue to grow. An application for a new bank has recently been filed. The last application for a new bank charter was filed in 2007. There have been 12 conversions from a federal charter to a Tennessee state banking charter over the last 6 years.

Over the past five years total assets in the state banking system have increased from $44 Billion to $60 Billion, or approximately $3.2 Billion per year representing a 6.4% compound annual growth rate. While a portion of the growth can be attributed to national banks converting into the state system, we have also experienced banks leaving the state system, primarily due to merger activity. We anticipate the rate of asset growth within the state system over the medium-term to remain positive and within a range of 3% to 5% on an annualized basis.

Loan growth in Tennessee has accelerated measurably over the past two years. Loan growth rates, on average, were actually negative from 2010 through the end of 2012. Beginning in early 2013 annualized loan growth rates turned positive, but were nominal at or below 2%. Loan growth rates have increased subsequently each year and are currently on pace to exceed 7% by year-end 2016, which should continue over the next 12 to 18 months given current economic growth and a positive economic outlook in Tennessee.

The Department continues to develop and implement its Regulatory Balance mission for depository institutions. Department examiners seek to right size regulation to the merits of each institution and avoid a one size fits all approach in order to support the Governor's economic goals for Tennessee. The Tennessee banking system is critical to the state's economic vitality and the Department's balanced regulatory approach supports economic progress.

With respect to non-deposit companies, the Department has established a new risk focused examination program that establishes a risk profile on licensed locations so that we can focus more resources on companies that are high risk. The goal is to improve the operations of non-deposit companies by sharing risk assessment information. Specifically, the Department seeks the greatest access to credit for consumers within the bounds of the law and fair operations by non-deposit companies.

In an effort to support the efficient and effective regulation of financial institutions, the Department recently implemented Alternative Workplace Solutions (AWS) to reduce the office space that the Department is assigned by nearly 75%, avoiding over $450,000 in annual cost. Nearly 90% of Department staff are either a mobile worker working at a financial institution or working from home for some portion of each week. The expectation is that AWS will offer us a greater opportunity to retain employees and create more experience to further help us find regulatory balance.

Our experience indicates that financial literacy is one of the keys to dealing with the economic issues facing us today. The Department has initiated a number of activities in recent years. Public service announcements, workshops, consumer alerts, panel discussions, a quarterly financial literacy newsletter to all state employees and an effort to reach Tennessee teachers and students were all a part of this effort. The Commissioner serves on the board of the Tennessee Financial Literacy Commission. The mission of the Tennessee Financial Literacy Commission is to equip Tennesseans to make sound financial decisions when it comes to planning, saving, and investing. A financially literate public is a key factor in establishing a safe and sound system of financial institutions.

The Department is organized into 4 main divisions: Bank, Credit Union, Compliance, and Administration. Please refer to the Organization Chart (Exhibit C) in Question 4, for staffing information.

<u>Question 2:</u> Provide information about the department's revenues (by source) and expenditures (by object) for fiscal year 2015 and 2016.

<u>Answer:</u> The department's revenues for fiscal years 2015 and 2016 totaled $18.7M and $19.8M respectively. The department's expenditures for 2015 and 2016 totaled $17.7M and 17.0M respectively. Refer to Exhibit A.

<u>Question 3:</u> How does the department ensure its staff is operating in an impartial manner and that there are no conflicts of interest? If the department operates under a formal conflict of interest policy, please attach a copy of that policy.

Answer: The Department's Ethics Policy is attached as Exhibit B. This Policy applies to all employees of the Department. There are several provisions of this policy that address conflicts of interest by Department employees as well as a section on impartiality. All employees (except support staff) have to file an annual disclosure statement. In addition, all employees have to file an annual certification that they have read the Department's Ethics Policy. The Department has an ethics committee that is available to answer any ethical questions an employee has. The Department also provides regular ethics training to our staff. Further, T.C.A. Section 45-1-117 prohibits Department employees from receiving any gift, taking out a loan, or investing in any institutions regulated by the Department except for a few exceptions. Governor Haslam's Executive Order 20 would apply to department employees. In addition, all staff are required to sign the DOHR Code of Conduct.

The Department has created a Regulatory Balance training guide for our staff. This guide asks our examiners to act with integrity, to set goals and purposes, and to provide great service to the financial institutions we regulate. Regulatory Balance is a value system that helps direct our examiner's technical training as they examine institutions in a way to help the Department meet its mission. The guide calls on examiners to act with justice and do what is right. If we can achieve justice, we will achieve impartiality.

Question 4: **Please provide a current organizational chart for the department.**

Answer: A current Organizational Chart is attached hereto as Exhibit C.

Question 5: **What were the department's major accomplishments during fiscal years 2015 and 2016? Specifically address the accomplishments of each division as each carries out its assigned duties.**

Answer:

Bank Division Accomplishments:

This Division is charged with the regulation and supervision of state-chartered financial institutions such as state-chartered banks, savings banks, trust companies, savings and loan associations, credit card banks, and business and industrial development corporations (BIDCOs). In order to more effectively carry out its responsibilities this Division is partitioned into four sections: Bank Examination Section, Financial Analysis Section, Application Section and Trust Examination Section. This Division is supervised by an Assistant Commissioner who reports directly to the Commissioner.

Through the process of on-site examinations and visitations, as well as off-site reviews, the Bank Examination Section monitors each financial institution under its jurisdiction for safety and soundness and/or compliance with statutory requirements.

During both fiscal years, the Department examined all banks within statutory timeframes in collaboration with the FDIC and Federal Reserve. Additionally, we ensured that all banks that were rated less than satisfactory were operating under an enforcement action within a reasonable timeframe and ongoing monitoring continues to be conducted. The Department has a tested and proven regulatory process led by an experienced senior management team. Our examiners receive training identical to that received by FDIC and Federal Reserve examiners, while our examiners also have an economic development perspective residing in or near the communities in which they examine banks. To further assist in this endeavor, the Department has compiled a Regulatory Balance manual for staff to assist with guiding our personnel in properly enforcing regulation with an approach to crafting oversight of institutions based on the institution's unique structure and risks. This allows examination personnel to ensure the safety and soundness of an institution, while at the same time recognizing the unique characteristics of each regulated institution within the State. This regulatory balance approach is not about applying a "one size fits all" examination approach, which can lead to the suppression of economic development within the State, but an approach of examining each bank on its own merits.

The Department maintains written, formal examination agreements with the federal regulatory agencies, which guide our cooperative supervisory programs. By law, each bank is examined at least once every 18 months, usually in an alternating schedule with the bank's primary federal regulator. Large or problem banks are moved into a 12-month examination schedule and are typically examined on a joint basis with the federal regulator. Onsite examinations represent a snapshot assessment of an institution's financial condition. Additionally, problem banks necessitate onsite visitations in the interim to assess the bank's condition and management's progress in addressing noted issues. On a quarterly basis, each Tennessee bank is reviewed offsite to detect any changes or outliers with each bank's examination schedule adjusted as warranted. The basis for this offsite analysis is generally comprehensive financial data provided quarterly in compliance with federal requirements.

The Bank Division employs a system of progressive discipline. When a bank shows minor weaknesses, we will seek the bank's Board of Director's cooperation in instituting either a Board Resolution or Memorandum of Understanding. In the event such informal actions are unsuccessful, formal actions may be required such as the issuance of a Written Agreement or an Order to Cease and Desist.

The Application Section is responsible for the review and analysis of all applications made to the Department for new banks, trust companies, savings and loan associations, credit card banks, savings banks, and BIDCOs. In addition, this Section analyzes all applications for mergers, acquisitions, branches, relocations, purchases and assumptions, and expanded activities. The application review process may include on-site visitations and investigations, as well as in-house analysis of financial data provided by the applicant. The goal of this Section is to identify any initial concerns which may forewarn significant problems.

The Applications Section met all statutory deadlines for the processing of all applications submitted to the division during Fiscal Years 2015 and 2016. During Fiscal Year 2015 there was one new trust company opening. In Fiscal Year 2016, there was one institution that converted into the state banking system from the national banking system and one new trust company opening.

The Financial Analysis Section works closely with the other three operating sections of this Division. Financial analysts oversee a portfolio of financial institutions and provide research and analysis assistance in addition to support on special projects.

The Trust Examination Section is responsible for the supervision of the trust departments of state-chartered banks and independent state-chartered trust companies. The examination of trust departments and trust companies requires broad knowledge of the laws and regulations relating to private and corporate trusts and estates, as well as, myriad of investment vehicles available.

The Department received its sixth re-accreditation by the Conference of State Bank Supervisors (CSBS) in 2014. Re-accreditation of the Department is conducted every five years and includes a review of administration and finance, personnel, training, examination, supervision and legislative functions.

Additional accomplishments specific to Bank Division for FY '15 & '16:

- In June 2016, the Department conducted a joint TEMA/TDFI Disaster Exercise which included both Federal and State chartered institutions. The banks and credit unions involved ranged from some of the largest to some of the smallest in Tennessee from Mountain City to Memphis. Common feedback received from these institutions was a greater awareness of TDFI and TEMA's availability to assist them in the event of an emergency. Financial institutions obtained a better understanding of the IT resources that will be required in the event of an emergency in order to restore operations. The Department's assistance in the event of a disaster is meant to protect, empower and enable financial institutions to help their employees, customers and local communities to recover economically as quickly as possible.
- Survey on Regulatory Balance - The Department sought an independent third party to survey all state-chartered banks and credit unions to see what they thought about the Department's regulatory balance philosophy. The survey results indicated that institutional managers had a very positive perception of the Department and its mission-based performance. Bank and credit union managers across Tennessee's three regional divisions gave the Department high ratings in terms of its knowledge of their institutions and the contributions they make to local communities. Likewise, the Department was highly regarded in terms of sustaining open lines of communication, providing objective examinations and reports, and engaging in effective regulatory oversight consistent with institutional and economic success. Relatedly, the Department ranked very high in the areas of accessibility, responsiveness, fairness, and professionalism. Written comments supported the statistical findings as respondents expressed a general appreciation of the professionalism and standard of performance maintained by the Department. A copy of the survey is attached hereto as Exhibit D.
- The Bank Division added/filled three new positions during this period:
    - The Bank Division Training Coordinator provides training directly and facilitates training of Bank Division personnel as we strive to maintain a team with the specialized expertise necessary to achieve our mission. Such training provided by the Bank Division now incorporates a focus on regulatory balance designed to ensure safety and soundness while promoting economic development for all Bank Division personnel from new employees to senior personnel, which is beyond what is provided by federal training alone

  - The Bank Division has also added the position of Consumer Compliance Liaison. This consultative position assists Tennessee banks in achieving compliance with applicable laws and regulations by staying abreast of changes and trends in laws, and regulations as well as their application. The Liaison also seeks to influence, where possible, the establishment of laws, regulations and their application to ensure the promotion of consumer protection while encouraging institutions to provide access to credit.
  - The Bank Division also added an Applications Analyst intended to provide an additional financial analysis resource for the processing of Bank Division applications in order to further expedite their processing.
- A legislative change found at Public Chapter 714 also occurred during this period. This change expanded the definition of "family" for private trust companies making Tennessee even more attractive to the private trust company industry.
- New processes have been set up for most of the applications submitted to the Bank Division to be accepted electronically and for replies to those applications to be provided electronically as well.
- The Bank Division has implemented a consultative initiative where we share best practices and helpful information with regulated institutions. Thus far, bank division examiners have shared information regarding cyber security, as well as information regarding the new consumer compliance liaison position of the division.
- We continue to hear from our institutions that access to the ultimate decision maker of their regulatory agency is one of the greatest benefits of a state charter. The Department maintains an open door policy and encourages institutions to meet with the Commissioner and staff whenever we may be of assistance. For many years, Commissioner Gonzales has been meeting with management and boards of institutions to hear directly how the Department can better partner with them in meeting their mission.
- The largest state chartered bank regulated by the Department has surpassed $10 Billion in assets. As a result, a new supervisory approach and "continuous" examination process is needed to coordinate with federal exam practice. As a result, the Department has established two new positions to ensure continuous management and oversight of the large and complex state-chartered banks.
- The Bank Division continues to make efficiencies in exam turnaround times a priority and strives to meet goals in this area.

Credit Union Division Accomplishments:

The Credit Union Division has the legal responsibility for assuring the Tennessee state-chartered credit union system operates on a safe and sound basis, while giving institutions the opportunity to contribute to the economic progress of Tennessee and the nation. In its supervisory role, the Credit Union Division periodically examines the financial soundness of all state-chartered credit unions and one corporate credit union. Credit Union examiners perform evaluations of each institution's assets, liabilities, income and expenses; monitor compliance with governing laws and regulations; and rate the effectiveness of the institution's management. The adequacy of capital is assessed to assure the protection of depositors. In addition, examiners review the information technology functions of state-chartered financial institutions for compliance with generally accepted information technology practices and for adherence to departmental regulations. The applications director for the Bank Division also oversees applications filed by credit unions.

During both fiscal years, the Department examined all credit unions within the statutory time frames. Like their counterparts in the bank division, all credit unions that were rated less than satisfactory were placed under an enforcement action and subjected to ongoing monitoring.

Examinations are achieved through routinely scheduled examinations performed by field examiners. Some examinations are performed jointly with the NCUA (National Credit Union Administration). The Credit Union Division meets annually with the NCUA to determine which credit unions will have joint examinations. Like bank examinations, credit union examinations are focused on providing an accurate assessment of the condition of state credit unions. Credit Union examiners also require years of specialized training. Each examiner is trained on the Department's regulatory balance philosophy and is asked to make judgments based on that philosophy.

Additional Credit Union Division Accomplishments:

- The Credit Union Division was reaccredited by the National Association of Credit Union Supervisors in FY 2015.
- The Credit Union Division fully implemented a new funding model in FY 2016 which allowed the Division to reduce its budget by $250,000.00. The funding model is designed so that the department only collects enough fees to adequately supervise and regulate state-chartered credit unions.
- In conjunction with the Department's implementation of Alternative Workplace Solutions (AWS), the Credit Union Division has imaged most records so that examiners in the field now have easy access to all credit union records.
- The NCUA recognizes the relatively favorable risk profile of Tennessee credit unions and the ability of the TDFI to assess the condition of credit unions. As a result, the number of joint exams has reduced from 58 in CY 2014, 45 in CY 2015, and 13 in CY 2016. This reduces regulatory burden on state-chartered credit unions.
- The Credit Union Division has exceeded its goal of getting reports of examination out to credit unions in less than 23 days.
- The Credit Union Division also met its goal to increase examiner experience. Examiner experience is critical to finding regulatory balance as we ask examiners to make important judgments about safety and soundness of institutions while being mindful of economic development.

Compliance Division Accomplishments:

The Compliance Division licenses check cashers, payday lenders, mortgage brokers, servicers and lenders, mortgage loan originators, money transmitters, industrial loan and thrift lenders, title pledge lenders, and flexible credit lenders. Each of these companies is subject to an annual licensing renewal requirement. In addition, the department applies a risk-based examination program to more frequently examine those lenders who pose the greatest risk of harm to the public.

Risk-Focused Exam Program

- The Department licenses many of its regulated entities through the Nationwide Multistate Licensing System ("NMLS"). The NMLS is a national licensing system and repository of information, including enforcement activity and consumer resource functionality, in which all 50 states and U.S. territories participate. The NMLS provides regulated industries the ability to license themselves, in the respective or multiple states in which they conduct business, and renew licenses through an internet-based electronic real time system. The Department was one of the original states in 2004 that participated as a working group member in creation of the NMLS under the auspices of the Conference of State Bank Supervisors.
- In July, 2013, the Department implemented a risk-focused examination scheduling program. The overarching purpose of the program is to focus available examiner resources on the regulated non-depository financial institutions that pose the greatest risk of potential harm to consumers. In other words, to focus regulatory efforts where there appears to be the greater risk to consumers. Secondarily, the program is designed to allow well managed institutions to serve their customers and contribute to the economic growth of their communities by extending the time between examinations. The categories for exam scheduling purposes are "Low", "Moderate", and "High". Examinations are scheduled according to the risk rating of each licensee. Licensees with a risk scheduling rating of "High" will be scheduled for examination on a more frequent basis than licensees with a risk rating of "Low" to "Moderate". For fiscal year ending June 30, 2016, the CFG goal of 100% of High Risk licensees examined during the year was accomplished as has been the case each successive year since program inception. An indicator of program success is in the migration of High Risk locations to other risk categories of Moderate or Low. We have observed a decline in the number of High Risk locations, over a three year period from 516 to 503 to 420. It should be noted that the figure of 420 does not include the new Flexible Credit industry. The Department is currently in the data gathering and analysis stage with regard to Flexible Credit lenders. Under another CFG goal, the Department has realized a reduction in the turnaround time in delivery of mortgage exam reports to licensees; that is, the period of time between the date an examiner exits the examination and the date that a written report of findings is delivered to the licensee. The CFG goal of a turnaround time on delivery of mortgage exams was set at 5.5 days. At fiscal year-end, the turnaround time for delivery of mortgage exams was 3.3 days.
- In November, 2010, the Department was recognized for leadership in the regulation of the mortgage industry receiving accreditation by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators. At the time, Tennessee was only the fifth state agency to be accredited for regulatory oversight of the mortgage industry. In December, 2014, the Department was re-accredited and received an overall rating score of 92.1% on a scale of 100.
- In 2016, the Department commissioned Tennessee Tech University to conduct a survey of all licensed non-depository institutions regulated by the TDFI. The survey was commissioned in

support of the Department's mission to create an environment for the greatest access to credit within the bounds of the law and fair operations of non-deposit companies. The survey was intended to garner industry perceptions of department communications, the risk-focused examination program, reporting and licensing processes of the TDFI and the funding model for non-depository supervision. The overall results of the survey were positive. Attached hereto as Exhibit E is a copy of the survey.

- During the subject period, department staff served on various multistate regulatory bodies including the Nationwide Multistate Licensing System ("NMLS"), Multistate Training and Education Board, and the Multistate Money Transmitter Examination Team. The Department also serves on a multi-agency task force regarding suspicious activity reports ("SAR") related to possible money laundering and mortgage fraud. The SAR team includes federal, state and local agencies that work cooperatively on this Task Force.
- In March, 2016, the Department issued to the Governor's Office and the General Assembly a report on the state of the title pledge industry in Tennessee which represents a biennial analysis and recapitulation of the general operating results of the industry. Historically, the report has been recognized as one of the most extensive and comprehensive analyses of the title pledge industry in the country.
- In FY 2016 the Department fully implemented a new funding model whereby we assess each licensee an annual supervision fee such that we only call in enough funds to adequately regulate the non-depository institution supervised by the Compliance Division. This new funding model is important in this volatile environment for non-deposit companies as it allows the Department to deal with wide swings in licensee population numbers without having to be forced to hire or lay off employees due to these swings.

Administrative Division Accomplishments:

In January, 2016 the Department implemented AWS (Alternative Workplace Solutions)

2016 CFG Accomplishments – AWS Implementation

- Savings- Shifting 88% of our work force to an AWS environment enabled us to reduce our footprint 26K square feet translating into $450K of savings that can be redirected to other priorities.
- Business Continuity – 37% reduction in the utilization of sick leave (did not include FMLA usage)
    - From 1/1/15 - 6/30/15 – staff utilized 5367.9 hours of sick leave
    - From 1/1/16 – 6/30/16 – staff utilized 3364.5 hours of sick leave
- Talent Management – A flexible work environment helps us retain our most experienced staff and recruit new talent from all across the state, strengthening our regulatory operations teams.

- Imaging – Before AWS, only one division was taking advantage of electronic imaging of internal documents. Now, all divisions have incorporated electronic records into their area, reducing our need for storage space.
- Increased productivity – Reducing weekly commute times, being able to access electronic records and taking advantage of communication tools like WebEx.
- Security – We are working more securely by accessing electronic records. Secured communications are also helping to lay a foundation for disaster preparedness. A disaster recovery exercise with TEMA and financial institutions in June reflected that AWS puts the Department in a better position to continue normal operations in the event of a disaster.

__Question 6:__ What reports does the department prepare on its operations, activities and accomplishments and who receives these reports? Please feel free to attach copies of these reports.

__Answer:__ Pursuant to T.C.A. § 45-1-119 the Department issues an annual report within sixty days of the end of each calendar year containing all required information and makes those reports available to the General Assembly. Reports are posted to the Department's website after the Governor orders that the reports be published. The department notifies all members of the legislature by email that the report is available on the Department's website or that the Department will provide them with a hard copy of the report upon request. A copy of the 2015 report is attached as Exhibit F. The 2016 Annual Report will be completed within 60 days of the end of the 2016 calendar year.

Some of the Acts the Department administers may have requirements for the Department to report items annually. For instance, the BIDCO Act at T.C.A. § 45-8-225 requires the Department to report certain accomplishments of the industry on an annual basis. This information is included in the Department's annual report.

The Department prepares a Financial Integrity Act Report that is filed annually with the Department of Finance and Administration.

Pursuant to T.C.A. § 45-15-108(e) the Department submits a biennial report to the General Assembly that includes an analysis of the rates and terms of title pledge loans and the reasonableness and appropriateness of those rates and terms. Attached as Exhibit G, is the 2016 Title Pledge Report.

The Department provides monthly reports to the Governor's office on the status of where we are on all customer focused government goals. The information regarding our progress on our key operational goals are then included in the transparent Tennessee website. Attached as Exhibit H, is the Transparent Tennessee information as of the end of FY 16.

__Question 7:__ Has the department promulgated rules? If so, please cite the reference.

__Answer:__ The Department has not promulgated any new rules in fiscal year 2015 or 2016. However, we are in the process of conducting an internal review of all rules to see whether any rules should be amended to reduce regulatory burden. On August 30, 2016 Rule 0180-25 was repealed. This rule outlined the assessment fee process for credit unions. This rule became unnecessary due to the 2015 amendment to T.C.A. § 45-4-1002 which created a new process to fund the Credit Union division.

Question 8: Describe any items related to the department that need legislative attention and your proposed legislative changes.

Answer: The Administration is currently in the process of evaluating potential legislation for the upcoming session.

Question 9: Should the department be continued? To what extent and in what ways would the absence of the department affect the public health, safety, or welfare?

Answer: The Department should be continued. The condition of financial institutions and public confidence in the Tennessee banking system is a constant mission for the Department.

Achieving a delicate balance of an appropriate level of regulatory oversight while allowing credit to flow and economic growth to occur, is the mission of the Department. As the chartering authority and "local" regulator, the Department has a unique view and understanding of the state banking system. We work closely with our federal partners, the FDIC, Federal Reserve and the NCUA, who rely on state regulators to share in the regulatory effort. These federal agencies establish nationwide standards for consistency, but it is the application of those broad standards with the assistance of state regulators who know local conditions that helps to ensure safety and soundness while allowing banks and credit unions to meet the needs of their communities.

The Department has an excellent working relationship with our primary federal partners: The FDIC, Federal Reserve and the NCUA. However our missions are somewhat different. While the federal agencies primarily are concerned with preventing any problem institutions, the Department has tasked its bank and credit union examiners with the extra challenge of looking for a balanced regulation on an institution by institution basis to allow institutions to serve their communities. If there are problems, we will deal with those problems without impacting the entire industry. The easier thing to do is to create more regulation to apply to all institutions, whether they are the best, or the problems. We ask our examiners to do the hard work of dealing with each institution on its own merits while permitting well managed institutions to serve their communities with the least amount of burden. Whatever regulation is needed will be provided, but the least amount of government intervention to accomplish the desired result is always the goal. That is not necessarily the federal approach. Commercial real estate lending is a good current example. There are a number of banks taking advantage of opportunities and stimulating economic development. We are urging our federal partners to not set one size fits all arbitrary limits on this activity, but make judgments on this activity on an institution by institution basis.

Should the Department sunset and not continue, Tennessee would lose some ability to control its own economic destiny to the extent we would lose any ability to determine who enters the banking system in the state and how those institutions are permitted to operate. Community banks and other local institutions exemplify economic freedom through local decision making. Without local regulators that can be held locally accountable, federal regulators might have little incentive to find regulatory balance. While federal regulators are strongly incentivized to try to prevent all failure, the TDFI seeks a balance. We will ensure standards of prudent operations along with permitting prudent risk by institutions. While no one wants failure, and Tennessee had relatively few failures compared to its neighbors in the Southeast, we would rather see a few market failures than trying to have no failures which would require substantially harsher regulation that could negatively impact the entire state's economy. We think our philosophy is exemplified in the statistic that a dozen federally chartered banks converted to a state bank charter over the last 6 years.

We seek to strengthen Tennessee's economy one community at a time, partnering with Tennessee financial institutions. Each financial institution is judged on its own merits, rather than more and more regulation for the industry, as a whole. To sunset the Department is to cede some of our economic freedom to Washington, D.C.

Question 10: Has the department developed and implemented quantitative performance measures for ensuring it is meeting its goals? If the department has developed and implemented quantitative performance measures, please answer questions 11 through 18. If the department has not developed quantitative performance measures, proceed to question 19.

Answer: The Department has developed and implemented quantitative performance measures to ensure we are meeting our key operational goals. The two key operational goals are:

- Operational Goal 1: Examine all state-chartered banks and credit unions as required by T.C.A. Section 45-2-1602 and 45-4-1002 during FY 2016 independently or jointly with the FDIC, Federal Reserve or the NCUA.

  This goal improves customer service by maintaining an efficient turnaround time on reports of examination which improves customer service directly to financial institutions and indirectly to the public. Examinations provide banks and credit unions with an independent measure of how to operate safely and potentially reduce cost. Any reduction in the cost of regulation improves customer service. Increasing the average experience of our bank and credit union examiners will also help reduce the turnaround time on exams. Our customers have requested more experience in our exanimation ranks. More experienced examiners are better equipped to find regulatory balance which provides better customer service.

  Streamlining the examination review process in order to reduce the turnaround time has allowed us to make more efficient use of our resources. Increasing the average experience of our bank and credit union examiners may allow us to reduce the number of days that our examination staff is on-site at a bank or credit union which would reduce costs and interruption of business to the entity being examined.

- Operational Goal 2: One hundred percent (100%) of all high-risk non-depository financial institutions regulated by the compliance division will be examined at least once each fiscal year in accordance with the Risk-Focused Exam Program. Those companies that present the least amount of risk will have their exam frequency extended beyond twelve months.

By risk-focusing exams, we are able to identify how to assist high-risk non-deposit companies to better serve citizens and to reduce exam burden on low-risk companies by reducing the frequency and cost of exams for low-risk companies.

Question 11: What are your key performance measures for ensuring the department is meeting its goals? Describe so that someone unfamiliar with the program can understand what you are trying to measure and why it is important to the operation of your program.

Answer: The key performance measures the Department used for determining whether we were meeting our goals in FY 2016 included:

- Goal: Examine all banks and credit unions as required
    - Measures:
        1. Maintain average turnaround time on bank exams of 45 days
        2. Average bank examiner experience of 11.0 years
        3. Median bank examiner experience of 6.5 years
        4. Maintain average turnaround time on credit union exams of 23 days
        5. Average credit union examiner experience of 13 years
        6. Median credit union examiner experience of 9.5 years

- Goal: Examine 100% of all high risk non-depositories
    - Measures:
        1. Average turnaround time on mortgage exam of 5 days
        2. Track percentage of non-deposit companies in the high-risk category (<10%)
        3. Average compliance examiner experience of 10.0 years
        4. Median compliance examiner experience of 10.0 years

The primary deliverables for the Department are the Reports of Examination we provide to the institutions we regulate at the conclusion of each examination. Therefore, we track the amount of time it takes the Department to issue the report of the examination after the conclusion of the exam. Getting reports of examinations to financial institution management sooner, allows them to take quicker action to correct any deficiencies noted. As noted earlier, regulatory balance (ensuring safety and soundness of depository institutions while giving them the opportunity to contribute to the welfare of communities) is fundamentally our driving mission and vision for depository institutions. For non-depository institutions such as finance companies, payday lenders, and non-bank mortgage companies, our guiding regulatory philosophy is to regulate in a way that gives the greatest access to fair credit within the bounds of the law for citizens that may not qualify or desire to go to a bank or credit union.

We request our field examiners to document examples of regulatory balance in order to give department leadership a view as to how our examiners are grasping the concept and applying it. We are receiving good feedback from our bankers as to how our examiners are applying this concept. The main thing we say is that we want our examiners to tell it like it is. Regulatory balance does not mean look the other way. We must give institutions our best judgment as to their condition and suggest measures that would be helpful, but it is also focused on helping institutions fulfill their purpose to the public. It is not to prevent all failures. It is to give banks the opportunity to succeed which means there is always a chance of failure. By its very nature, banking is a risky business. We cannot eradicate all risk because to do so would inhibit banks in their ability to contribute to the economy. In order to have the opportunity for success, there must be the possibility of failure.

Examiner experience is critical to finding regulatory balance as we ask examiners to make important judgments about safety and soundness of institutions while being mindful of economic development. That is why we measure the median and average examiner experience of our examination staff on an annual basis. We want to empower examiners to make judgments rather than recommend more one size fits all regulation that applies to all institutions regardless of risk profile.

With respect to non-bank payday lenders, car title lenders and other such lenders, the Department has established a risk focused examination program where we track the number of lenders who pose a higher risk to the public and their migration in and out of the high risk category. Similar to the depository institution examiners, experienced non-depository examiners make judgments with regard to an institution's risk profile.

Question 12: What aspect[s] of the program are you measuring?

Answer: The first key operational goal is to examine all state chartered banks and credit unions within the time frames required by statute. The Department continually monitors whether we are completing exams on banks and credit unions as required by statute. We have not experienced any concern with examining the institutions within the required time frame. However, we have experienced some opportunities to improve the time frame within which our reports of examination are provided to the institutions we regulate and that is why we developed the quantitative measurement with regard to examination turnaround time. In addition, having experienced examiners helps us to insure that examinations are completed timely.

The second key operational goal is to examine all high risk non-depository entities within twelve months. We have successfully examined all high risk entities in that time frame. The department tracks the percentage of high risk entities each year because the risk focused examination program's goal is to reduce the numbers of high risk entities over time.

Question 13: Who collects relevant data and how is this data collected (e.g., what types of information systems and/or software programs are used) and how often is the data collected? List the specific resources (e.g., report, other document, database, customer survey) of the raw data used for the performance measure.

Answer: Attached as Exhibit I is the internal procedure that outlines how the Bank Division calculates its report of exam turnaround time. This procedure identifies how the data is collected.

Attached as Exhibit J is the internal procedure that outlines how the Credit Union Division calculates its report of examination turnaround time. This procedure identifies how the data is collected.

Attached as Exhibit K is the internal procedure that outlines how the Compliance Division calculates its report of mortgage examination turnaround time. This procedure identifies how the data is collected.

The average and median examiner experience is calculated by a designated person in each division. The Bank Division only includes work experience as a bank examiner with the Department or with a federal banking regulator. The Credit Union Division only includes experience as a bank or credit union examiner with this department or experience as a bank or credit union examiner with a federal banking or credit union regulatory agency. The Compliance Division only includes experience as an examiner with the Department. An analyst in each division calculates the experience for each examiner at the end of each fiscal year. The only employees included in the calculation are the examiners who were employed as of the last day of the fiscal year that is being measured.

Attached as Exhibit L is the internal procedure that outlines how the Compliance Division calculates the percentage of high risk non-depository lenders included in the risk scheduling program.

Question 14: How is the actual performance measure calculated? If a specific mathematical formula is used, provide it. If possible, provide the calculations and supporting documentation detailing your process for arriving at the actual performance measure.

Answer:

- Attached as Exhibit M (1&2) are worksheets showing how the bank division calculates its report of examination turnaround time. Please note that on all of these exhibits attached in this section- the names and cities for all financial institutions have been redacted.
- Attached as Exhibit N is a worksheet showing how the credit union division calculates its report of examination turnaround time.
- Attached as Exhibit O is a sample worksheet showing how the compliance division calculates its mortgage company report of examination turnaround time.
- Attached as Exhibit P is a worksheet showing the average and median bank division examiner experience as of June 30, 2015.
- Attached as Exhibit Q is a sample worksheet showing how the Compliance Division calculates the percentage of high risk companies.
- Attached as Exhibit R is a worksheet showing the average and median credit union division examiner experience as of June 30, 2015.
- Attached as Exhibit S is a worksheet showing the average and median compliance division examiner experience as of June 30, 2015.

Question 15: Is the reported performance measure result a real number or an estimate? If an estimate, explain why it is necessary to use an estimate. If an estimate, is the performance measure result recalculated, revised, and formally reported once the data for an actual calculation is available?

Answer: All metric measurements use actual numbers and not estimates.

Question 16: Who reviews the performance measures and associated data/calculations? Describe any process to verify that the measure and calculations are appropriate and accurate.

Answer: The Department's internal auditor confirms the accuracy of bank and credit union report of examination turnaround time and the accuracy of the average and median experience of all examiners. The Compliance Division performs an internal review of the accuracy of the mortgage report turnaround time and the percentage of companies who are high risk. These items are tracked on an excel spreadsheet. The Department is in the process of working through STS to create a database which will help us better insure the integrity of the data involved in these measurements.

Question 17: Are there written procedures related to collecting the data or calculating and reviewing/verifying the performance measure? Provide copies of any procedures.

Answer: See response to Question #13.

Question 18: Describe any concerns about the department's performance measures and any changes or improvements you think need to be made in the process.

Answer: We are always looking for ways to improve our goals, metrics, measurements and milestones. Therefore, we have made some additions to the 2017 CFG goals/metrics. For instance, we are planning a cyber security exercise and training for the Department and depository institutions.

Question 19: Please list all department programs or activities that receive federal financial assistance and, therefore are required to comply with Title VI of the Civil Rights Act of 1964. Include the amount of federal funding received by program/activity.

Answer: None

Questions 20 – 25: N/A

Question 26: Please provide a breakdown of current department staff by title, ethnicity, and gender.

Answer: See Exhibit T.

<u>Question 27:</u> Please list all department contracts, detailing each contractor, the services provided, the amount of the contract, and the ethnicity of the contractor/business owner.

<u>Answer:</u> See Exhibit U.

EXHIBIT A			
EXPENDITURES BY OBJECT/ EDISON CATEGORY AND REVENUES SUMMARIZED BY SOURCE			
			Est.
		2015	2016
Account	Description	Actual	Actual
	Personnel	13,245,768.43	13,962,034.91
	Operational	4,432,675.86	2,999,765.41
	Total Expenditures	**17,678,444.29**	**16,961,800.32**
	State Appropriations	18,671,609.29	19,823,461.21
	Reserves	0.00	0.00
	Reserve - Unencumbered Bal	2,271,728.43	821,728.43
	Reserve - Capital Outlay	0.00	0.00
	Federal	0.00	0.00
	Other	3,186.84	9,866.90
	Total Funding	**20,946,524.56**	**20,655,056.54**
70100	Regular Salaries	9,407,184.03	9,992,136.28
70102	Longevity	171,800.00	181,000.00
70104	Overtime	112.50	0.00
70200	Benefits	3,666,671.90	3,788,898.63
	Subtotal Personnel	**13,245,768.43**	**13,962,034.91**
70300	Travel	587,646.61	677,243.41
70400	Printing and Duplicating	7,793.48	54,670.00
70500	Utilities and Fuel	0.00	0.00
70600	Communications	24,268.79	29,019.16
70700	Maintenance, Repairs, and Service	152.00	180.00
70800	Professional Services Third Party	212,413.04	229,780.28
70900	Supplies and Materials	26,165.06	29,154.82
71000	Rentals and Insurance	24,034.88	12,905.25
71100	Motor Vehicle Operations	1,984.70	855.29
71200	Awards and Indemnities	1,424,639.58	1,128.87
71300	Grants and Subsidies	0.00	0.00
71400	Unclassified	5,600.00	6,400.00
71500	Stores for Resale/Reissue/Mfg.	0.00	0.00
71600	Equipment	0.00	197.00
71700	Land	0.00	0.00
71800	Buildings	0.00	0.00
71900	Discounts Lost	0.00	0.00
72000	Highway Construction	0.00	0.00
72100	Training	85,906.47	112,496.00
72200	Data Processing	158,284.25	263,373.92
72500	Professional Services State Agencies	1,873,787.00	1,582,361.41
73100	Retirement of Debt	0.00	0.00
73200	Interest on Debt	0.00	0.00
73300	Trustee Fees	0.00	0.00
73500	Depreciation	0.00	0.00
73600	Loss on Disposal of Equipment	0.00	0.00
73700	Reallocations Plant Work Order	0.00	0.00
	Subtotal Operations	**4,432,675.86**	**2,999,765.41**
	Total Expenditures	**17,678,444.29**	**16,961,800.32**
85200	Reserve - Unencumbered Bal	2,271,728.43	821,728.43
85300	Reserve - Capital Outlay	0.00	0.00
85400	Reserves	0.00	0.00
86050	State Appropriations Bank Assessments	9,578,995.17	10,212,702.21
	State Appropriatins Other Bank Fees	588,813.86	238,600.08
	State Appropriatins Credit Union Supervision Fees	2,542,252.17	2,272,838.40
	State Appropriatins Other Credit Union Fees	0.00	900.00
	State Appropriatins Non-Depository Supervision Fees	5,775,211.00	6,952,658.68
	State Appropriations Non-Depository Penalties	186,337.09	145,761.84
	Total Appropriation	**20,943,337.72**	**20,645,189.64**
68001	Federal Revenue	0.00	0.00
68002	Federal Capital Grants	0.00	0.00
68012	Refund Prior Year Federal Expense	0.00	0.00
	Total Federal	**0.00**	**0.00**
68030	Counties	0.00	0.00
68040	Refund of Prior Year Local Expense	426.84	0.00
68050	Cities	0.00	0.00
68060	Non-Governmental	0.00	0.00
68070	Other State	0.00	0.00
68080	Current Services	360.00	660.00
68085	Interest Income	0.00	0.00
68090	Inter-Departmental	2,400.00	9,206.90
68095	Interdepartmental - CU	0.00	0.00
68200	Current Services - Licenses	0.00	0.00
68300	Current Services - Fines	0.00	0.00
	Subtotal Other Revenue	**3,186.84**	**9,866.90**
	Total Funding	**20,946,524.56**	**20,655,056.54**

Total Bank Surplus	$ 2,446,292.57			
Less Bank Rebate	$ 2,366,330.79			
		$ 79,961.78	$ 188,684.75	
Compliance	$ 2,657,455.60			
Add Funded From MTG Settlement	$ 149,110.63	$ 2,806,566.23	$ 2,806,566.23	
Credit Union	$ 137,860.68	$ 137,860.68	$ 137,860.68	
Funded From MTG Settlement				
General Fund Reversion		$ 3,024,388.69	$ 3,133,111.66	$ 108,722.97